



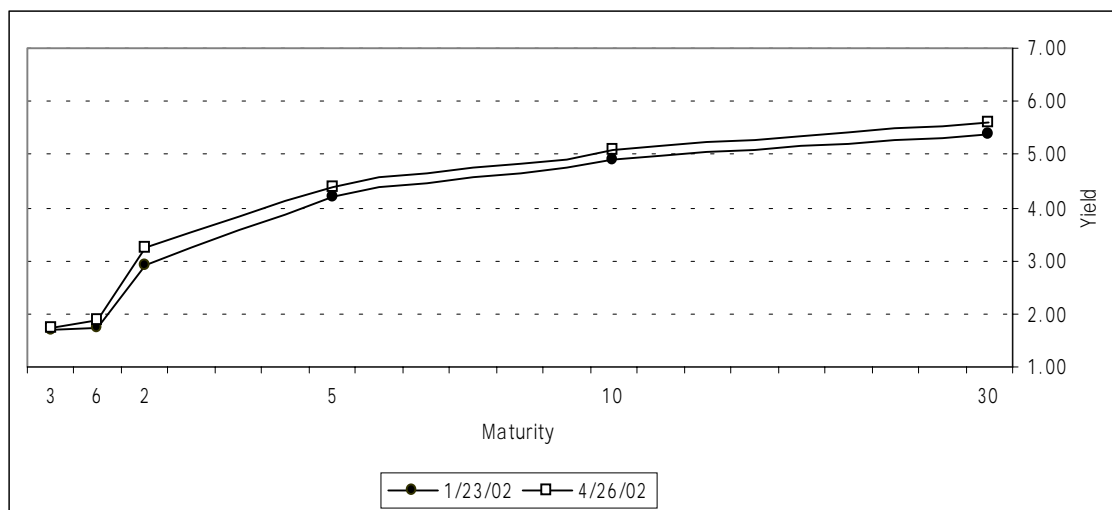
**MICHAEL J. MURPHY**  
*State Treasurer*

**First Quarter 2002**

# The QUARTERLY

## Local Government Investment Pool

### Historical Yield Curve January 23, 2002 vs. April 26, 2002



### Economy begins to show signs of life...

After entering a recession in March 2001, the economy appears to be on the road to recovery. Real GDP was revised up for the fourth quarter of 2001 from an annual rate of 0.2 percent to 1.4 percent, starting 2002 off at a higher level. And most recently, first quarter GDP growth of 5.8 percent was a significant improvement and higher than most economists had expected.

By comparison, the current recession has been rather mild. However, in measuring economic performance, there has been a major discrepancy between the consumer and business sectors. It seems the real recession has taken place in the business sector. While consumers, undaunted by the news of recession, have continued to borrow and spend, businesses have been cutting back capital spending, inventories, and personnel. Indeed, Fed Chair Greenspan noted in recent remarks to Congress that business investment is key to keeping this recovery on pace.

The index of Leading Economic Indicators, which forecasts turning points in the economy, was flat in February but edged up in March. Six of the 10 measures that make up the index rose in March, led by stock prices, the interest rate spread, and consumer expectations. This rise in the key gauge of economic activity suggests continued growth in the months ahead.

After a severe downturn, it looks as though the manufacturing sector is turning around. The Institute for Supply Management (ISM; formerly NAPM) manufacturing index, which had dipped in December, began to recover in January. The index then climbed sharply in February.

The broadest monthly indicator of economic activity, employment, held steady in January and February. Jobless claims then surged in March. Those figures were distorted, however, due to

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## Market summary

*from page 1*

the number of workers refiling claims for extended benefits. Unemployment numbers are expected to remain artificially higher through the end of the April reporting period.

For the first time since the fourth quarter of 2000, we have gone an entire quarter with no move by the Fed. After lowering the Fed funds rate from 6.50 percent to 1.75 percent between January and December 2001, the Fed decided it had done its part to boost the economy and further cuts were not necessary. Accordingly, the Fed funds rate was unchanged, at 1.75 percent, at the January and March meetings.

Of significance at the March 19 meeting was the move to a neutral bias. Throughout 2001, and even at the Jan. 30 meeting when the Fed held the funds rate steady, the bias was towards weakness. In other words, the Fed viewed the risk to its goals of price stability, e.g., low inflation and sustainable economic growth, as weighted towards weak growth. However, due to signs the economy was recovering, the Fed announced at its March 19 meeting "the risks are balanced with respect to the prospects for both goals", i.e., price stability and sustainable economic growth.

The implications of this statement for the funds rate is that the next change in the funds rate is likely to be an increase, i.e., tightening, which was widely anticipated by investors.

The question now becomes "When will the Fed begin tightening?" Two months ago, most investors believed the Fed would begin tightening at the May 7 FOMC meeting, and Fed funds would rise to the 3 percent level by year's end. However, recent data show the economy, while definitely on the rebound, is not growing as fast as anticipated. This, along with higher oil prices and constructive comments from Greenspan, has most investors now seeing the first tightening in June, August, or even later.

A change in investor expectations about the timing and pace of Fed tightenings has been evident in the bond market. The spread between the Fed funds rate and the two-year Treasury Note widened from 98 basis points (bp) in early January to 198 bp in late March, as investors became convinced the Fed would soon begin an aggressive tightening schedule. However, over the last month the spread has narrowed to 149 bp as investors have moder-

ated from that position.

The yield curve has changed little since the last newsletter was published (see chart on page 1). On the short end of the curve, we have seen a steepening. This reflects the view that, although the Fed has not yet started tightening, the market expects that it soon will. When compared to January, three-month rates are only 3 bp higher while two-year rates are 31 bp higher. On the longer end of the curve there has been a flattening, as two-year rates have risen more than 5-, 10-, or 30-year rates.

While the Dow has risen slightly over the last quarter, 9,714 on Jan. 22 to 9,940 on April 26, the NASDAQ has dropped from 1,883 on Jan. 22 to 1,671 on April 26.

The net return on the LGIP during the first quarter of 2002 ranged from 2.07 percent to 1.84 percent. Reminder: as we enter a time period where the Fed might begin to raise rates, the targeted Fed funds rate is a good proxy for estimating the LGIP rate in the future. For example, if the Fed tightens to 3.00 percent, you can expect the LGIP rate to also approach 3.00 percent. However, the average life of the portfolio will cause the LGIP rate to lag changes in the funds rate. Currently, the average life of the portfolio is approximately 55 days. As we anticipate the Fed to begin tightening, the average life of the portfolio will be shortened so we can respond as quickly as possible to the rising rates.

## TM\$ proves popular with LGIP participants

Since its launch in January, the Treasury Management System (TM\$) has become increasingly popular with LGIP. On average, about 60 percent of the LGIP's daily transactions are now initiated via TM\$.

TM\$ offers a convenient way for LGIP participants to view account information and allows authorized users to enter transactions on-line. TM\$ users can retrieve and print account history, account ledgers, and have immediate access to their statements of account.

If you are not currently using TM\$ and would like to, or if you have questions about the system, please contact Lisa Hennessy, interim LGIP administrator, at 1-800-331-3284.

## LGIP Advisory Committee

### Mary Dodge

Douglas County Treasurer  
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### Stan Finkelstein

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### Chuck Greenough

State Board for Community and Technical Colleges  
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### Mark Wyman

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## EVENTS

### Don't miss WFOA 2002

September is quickly approaching and you don't want to miss the Washington Finance Officers Association (WFOA) 2002 conference in Yakima. The class schedule is packed with useful information, including an entire investment track which progresses from investing basics to more advanced topics. There will be debt management, accounting and technology classes, too.

Want to know more? Visit the WFOA web-site at [www.wfoa.org/conferen.htm](http://www.wfoa.org/conferen.htm).

### Welcome new LGIP participants

Help us in thanking and congratulating our new LGIP participants who have become members in the first quarter of 2002:

*Chelan County PUD #1*

*City of Pomeroy*

*Roza Irrigation District*

*City of Tacoma*

*Town of Waterville*

## Minutes of March 22 advisory committee meeting

The LGIP Advisory Committee met March 22. A brief update was given on the net LGIP returns for December 2001 through February 2002. The LGIP has outperformed its benchmark by about 44 basis points (bp). The fed funds rate has been stable at 1.75 percent. The general consensus of investors is that the next move by the Fed will be a tightening, but when it will occur is unclear. The next Fed meeting is scheduled for May 7. The LGIP rate is about the same as the fed funds rate and it will increase after the Fed begins to tighten. The average life of the pool is about 60 days.

Treasurer Mike Murphy announced the expiring appointments of advisory committee members Rick Patrick, Paula Henderson, Stan Finkelstein and Mary Dodge. Patrick and Henderson were reappointed by Treasurer Murphy for three-year terms to expire on April 30, 2005. Finkelstein submitted a letter to Treasurer Murphy saying he would like to be re-appointed as the AWC representative to the LGIP advisory committee.

OST gave a brief report personnel changes in the Investment section. Tracie Kier, who was the LGIP Administrator, went on maternity leave in mid-November and has made the decision to remain at home with her daughter. Cristin Wilson, the LGIP portfolio manager, is on maternity leave until late June, when she will return to OST part-time, but not as the portfolio manager. Lisa Hennessy has assumed the interim duties of the LGIP administrator, and Doug Extine is managing the LGIP portfolio.

Kim Hurley of the State Auditor's office (SAO) gave a brief presentation on LGIP audit options. She described the four options available for obtaining an audit opinion on the LGIP: 1) No opinion; 2) Opinion issued by SAO; 3) Opinion issued by a CPA firm contracting through SAO; and 4) Opinion issued by a CPA firm relying on work performed by SAO.

The LGIP has chosen Option 4 in previous years, with Frost and Company as the CPA firm. Option 4 would be less costly than Option 3, but it would cost more than past years because of the cost of the SAO portion of the audit. Kim responded to questions and then left the meeting.

Advisory committee members reached consensus that Option 4 would be the best choice for the LGIP independent audit.

A review of the Fiscal Year 2002 budget was given. Expenses are essentially on target, slightly under the estimate for the fiscal year to date. The average balance of the LGIP so far this fiscal year, about \$5 billion, is much larger than was used to estimate the amount of fees that would be collected. Adjusting for actuals, the estimated rebate is now at \$1,189,690.

A brief update on the TM\$ project was given. OST is very happy with the TM\$ utilization rate. For example, 60 percent of transactions for one day were done via the Website. Overall, entities have been satisfied with the system. Mark Wyman suggested having an information line in the TM\$ system where entities could make comments, etc.

## It's a boy!

Cristin Wilson had a baby boy. Here are the details:

**Baby's Name:** Colby Clayton

**Birth Date:** March 23, 2002

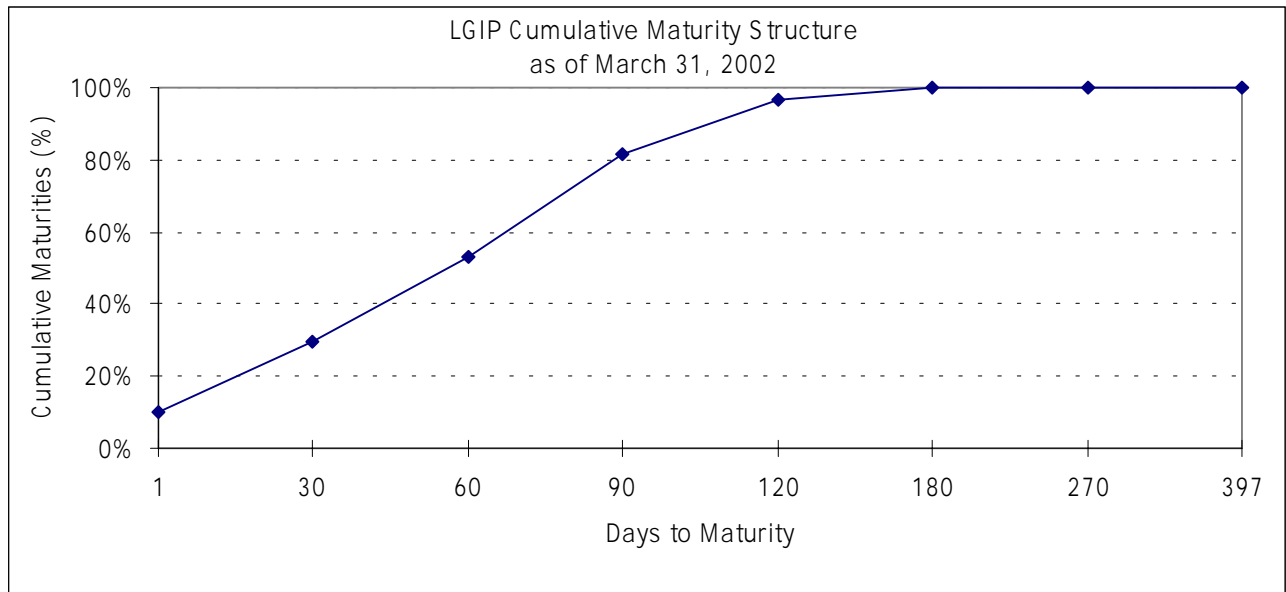
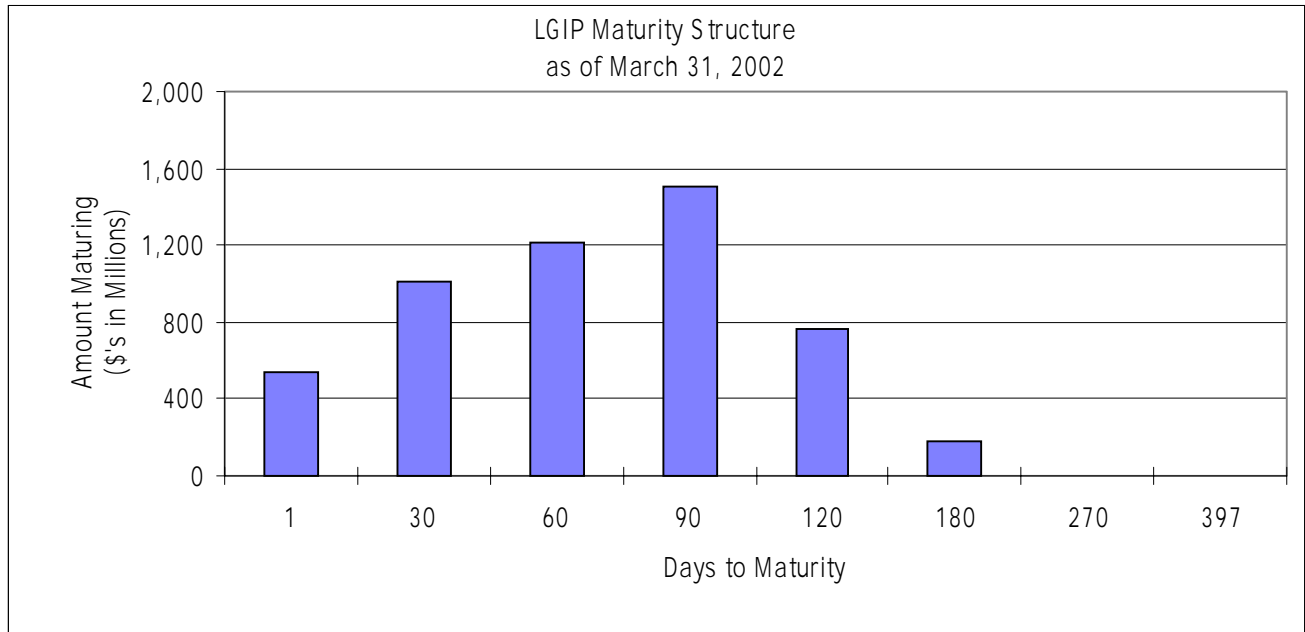
**Birth Time:** 2:35 p.m.

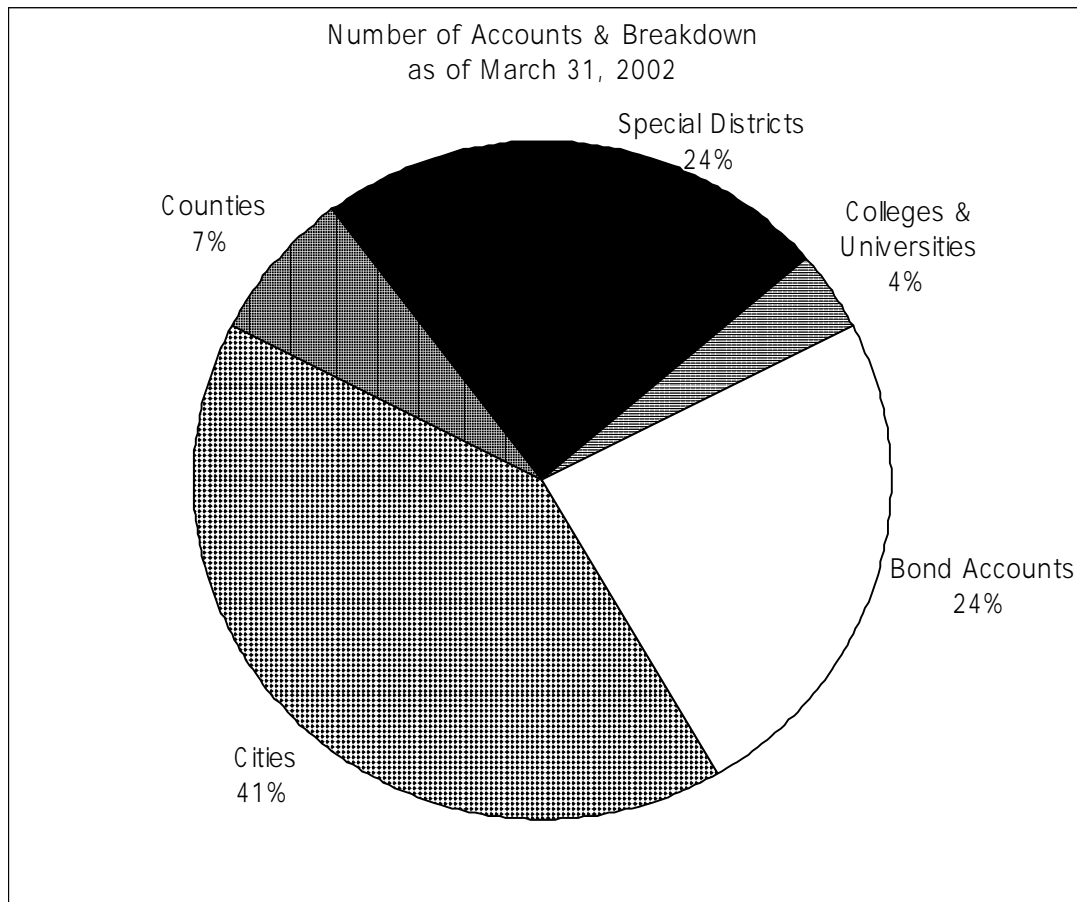
**Weight:** 9 pounds, 6 ounces

### LGIP Holiday Schedule for 2002

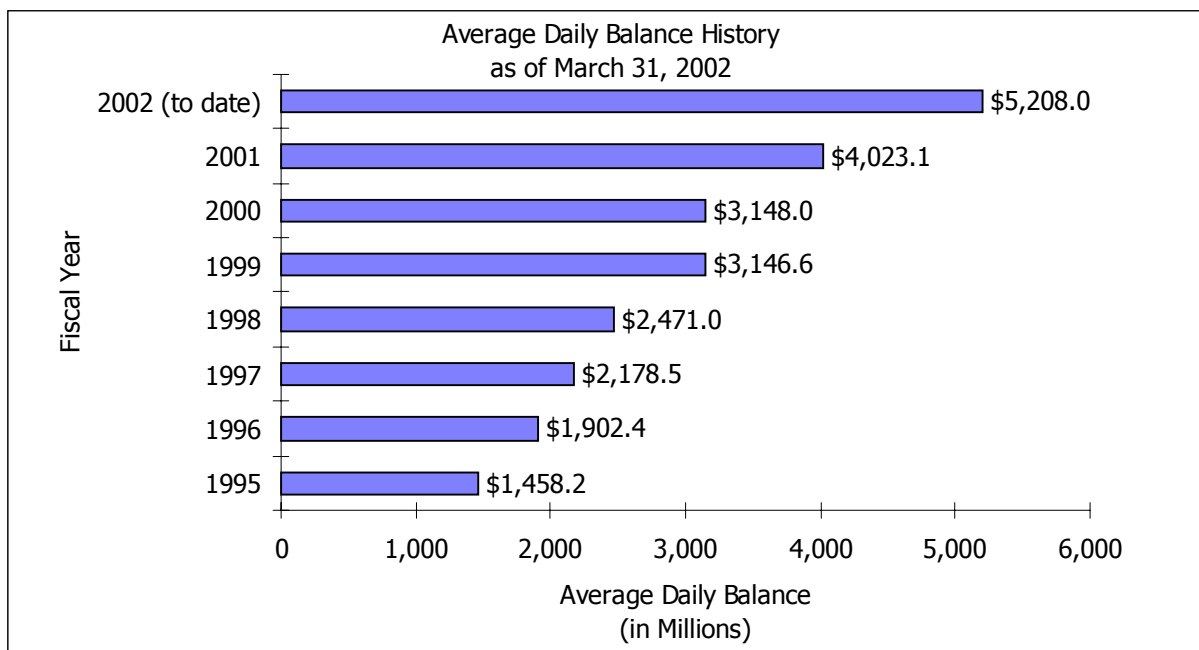
The Local Government Investment Pool will be closed on the following days:

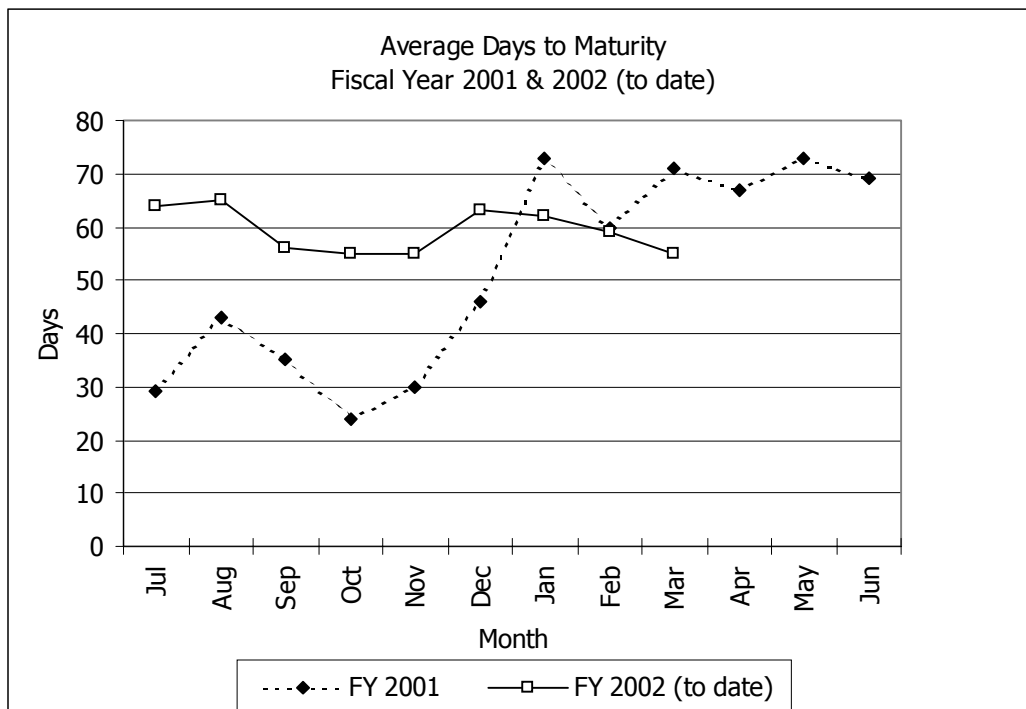
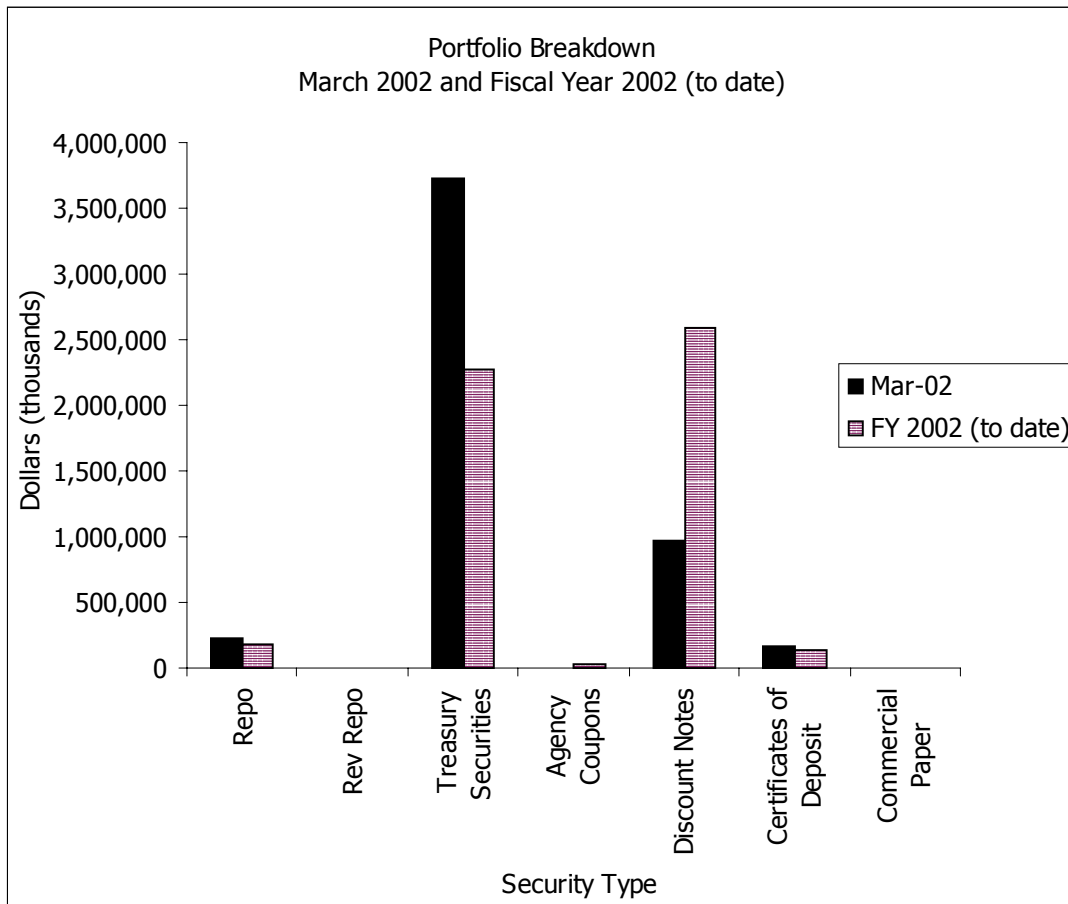
Monday	May 27	Memorial Day
Thursday	July 4	Independence Day
Monday	September 2	Labor Day
Monday	October 14	Columbus Day
Monday	November 11	Veteran's Day
Thurs/Fri	November 28-29	Thanksgiving
Wednesday	December 25	Christmas Day





*Total number of accounts: 544*





## **New procedures for faxing LGIP statements of account**

The monthly interest allocation cannot occur until the last day of the month. This has important ramifications for determining when you will receive your statement of account.

### **If the last day of the month is a business day:**

When the last day of the month is a business day, earnings interest will be allocated as soon as all pending transactions have been verified as having occurred. In most cases this is done during the afternoon of the last day of the month. Statements will be faxed beginning at 5 p.m. However, statements will be available via TM\$ as soon as the interest allocation process is completed. At that time, statements are printed and mailed to those entities receiving their statements by U.S. mail.

### **If the last day of the month is not a business day:**

When the last day of the month is **not** a business day, interest allocation will occur on the first business day of the next month. Accordingly, statements will be faxed on the first business day of the next month. While we anticipate faxing to begin as early as 8 a.m., it takes about six hours to fax all the statements. Consequently, it may be late in the day before you receive your faxed statement. We are currently working on ways to streamline the faxing process.

### **What is the fastest way to get my statement of account?**

The fastest way to receive your LGIP statement of account is via TM\$. Statements will always be available immediately after the interest allocation occurs. If you do not have access to TM\$ and want to begin using it, contact Lisa Hennessy, interim LGIP administrator, at 1-800-331-3284.

Also, if you access your statement of account through TM\$ and no longer require a fax or mailed copy, notify the LGIP. This will greatly reduce the cost and time of unnecessary faxing and mailing of statements.

Thanks for your cooperation.

# Washington State Local Government Investment Pool

## Position and Compliance Report

### as of March 31, 2002

(Settlement Date Basis)

### LGIP Portfolio Holdings

	Cost	Percentage of Portfolio
Repurchase Agreements	\$ 220,000,000	4.24
U.S. Treasury Securities	4,019,186,498	77.39
U. S. Agency Bullets	.....	0.00
U.S. Agency Generic Floaters	.....	0.00
U.S. Agency Discount Notes	510,075,145	9.82
Certificates of Deposit	444,050,000	8.55
Bankers Acceptances	.....	0.00
Commercial Paper	.....	0.00
Reverse Repos	.....	0.00
<b>* Total Excluding Securities Lending</b>	<b>\$ 5,193,311,644</b>	<b>100.00</b>

### Securities Lending Holdings

	Cost
Repurchase Agreements	\$ -
Banker's Acceptances	
Commercial paper	
<b>Total Securities Lending</b>	<b>-</b>

**Total Investments & Certificates of Deposit**      \$ 5,193,311,644

### Policy Limitations

*The policy limitations include investment of cash collateral by a securities lending agent calculated as percentages of the portfolio holdings Total Excluding Securities Lending.\**

<u>Size Limitations</u>	Holdings	Percentage of Portfolio	Policy Limitations Percentage
Certificates of Deposit	444,050,000	8.55	10%
Bankers Acceptances (BA)	.....	0.00	20%
Commercial Paper (CP)	.....	0.00	25%
Securities With Higher Volatility	.....	0.00	10%
Repos Beyond 30 days	.....	0.00	30%
Aggregate BA & CP Holdings	.....	0.00	35%

### Leverage (30% Total Limit)

Securities on Loan (dollars out on loan)	\$.....	
Reverse Repos	.....	
<b>Total Leverage</b>	<b>\$.....</b>	<b>0.00%</b>

### Maturity Limitations

	<u>Currently</u>	<u>Policy Limitations</u>
Portfolio Average Life	57 days	90 days
Maximum Maturity	180 days	397 days
Maximum Maturity of Repo	1 day(s)	180 days
Maximum Maturity of Reverse Repo	0 day(s)	90 days
Average Life of Reinvestment of Cash by Lending Agent	0 day(s)	14 days



## Policy Limitations (Continued)

### Repo Limits Per Dealer

	<u>March 31, 2002</u>	<u>Total Repo Percentage (20% limit)</u>	<u>Term Repo Percentage (10% limit)</u>	<u>Projected Redemptions 4/1/02</u>	<u>Projected Position 4/1/02</u>
Banc of America Securities LLC	\$.....	0%	0%		.....
Bank of New York	.....	0%	0%		.....
Barclays Capital Markets	.....	0%	0%		.....
Bear Stearns & Co.	.....	0%	0%		.....
CS First Boston	.....	0%	0%		.....
Chase Manhattan	.....	0%	0%		.....
Daiwa Securities America Inc.	.....	0%	0%		.....
Dresdner Securities USA	.....	0%	0%		.....
Fuji Securities	.....	0%	0%		.....
Greenwich Capital Markets Inc.	.....	0%	0%		.....
Lehman Brothers Inc.	220,000,000	4%	0%	220,000,000	.....
Merrill Lynch & Co., Inc.	.....	0%	0%		.....
Morgan Stanley	.....	0%	0%		.....
Nesbitt Burns	.....	0%	0%		.....
Nomura Securities Intl Incorporated	.....	0%	0%		.....
Paribas Corporation	.....	0%	0%		.....
Prudential Securities	.....	0%	0%		.....
Salomon-Smith Barney	.....	0%	0%		.....
UBS Warburg LLC	.....	0%	0%		.....
<b>Total</b>	<b>\$ 220,000,000</b>			<b>220,000,000</b>	.....

### Issuer Limitations

#### **\*\*** Commercial Paper

<u>Cost</u>	<u>Percentage (5% limit)</u>	<u>Rating (A1/P1 or Better)</u>
-------------	----------------------------------	-------------------------------------

There was no commercial paper holdings as of 3/31/2002.

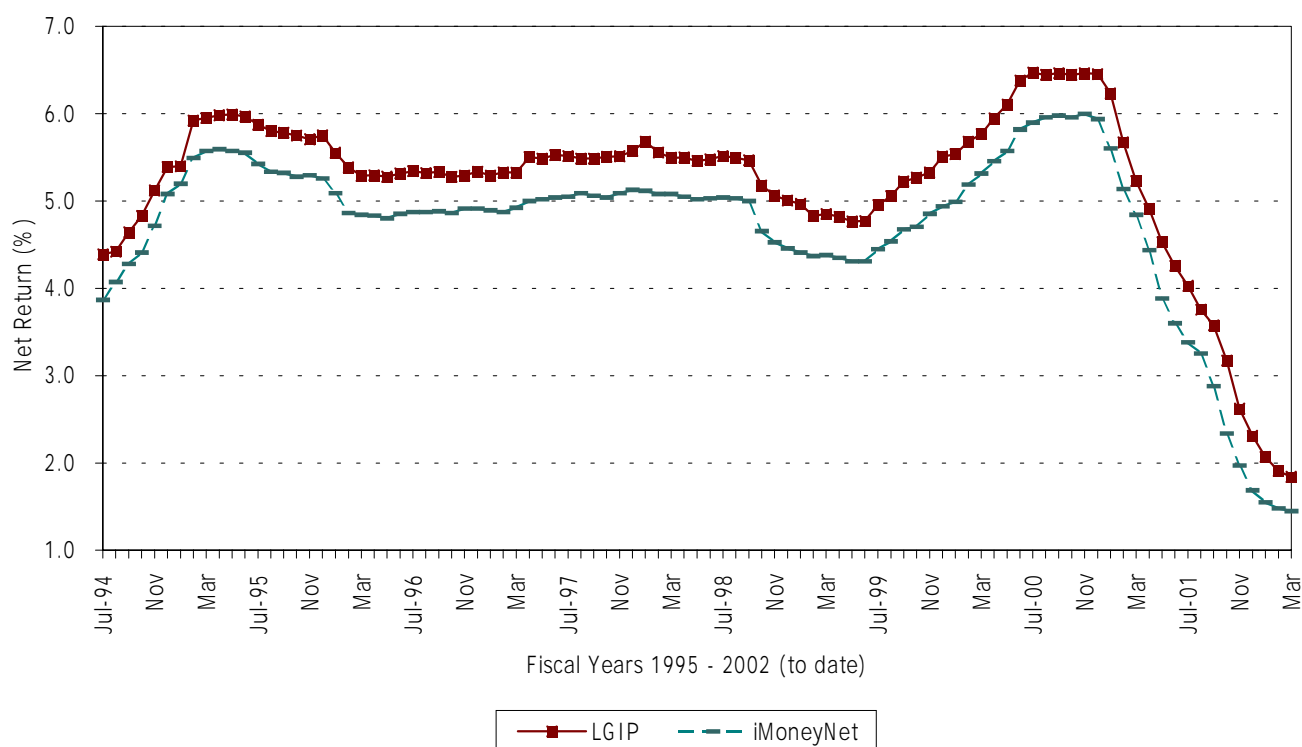
#### Banker's Acceptances

There was no banker's acceptance holdings as of 3/31/2002.

**\*\*** These are the limitations of the formal Investment policy. However, operating guidelines place limits of 3% per issuer.

## LGIP Performance Comparison

**iMoneyNet, Inc., Government Only/Institutional Only  
versus  
Local Government Investment Pool**



### Net Rate of Return Fiscal Years 1995 – 2002 (to date)

Average Net Rate of Return of Government Only/Institutional Only Money Market Funds, Money Market Insight, iMoneyNet, Inc., Westborough, MA.

NOTE: Rates are calculated on a 360-day basis.

The above comparison shows how the LGIP has performed relative to its benchmark since July 1994. This benchmark is the iMoneyNet, Inc., Government Only/Institutional Only Money Market Funds, which is comprised of privately managed money market funds similar in composition and investment guidelines to the LGIP.

The LGIP net rate of return has outperformed its benchmark since July 1994 by an average of 48.0 basis points. This translates into the LGIP earning \$106.55 million over what the average comparable private money fund would have generated.

# Local Government Investment Pool

## STATEMENT OF NET ASSETS

March 31, 2002

### Assets

Investments, at Amortized Cost:	
Repurchase Agreements	220,000,000
U.S. Agency Discount Notes	510,075,145
U.S. Treasury Securities	<u>4,019,186,498</u>
Total Excluding Securities Lending, Securities Purchased But Not Settled & Securities Sold But Not Settled	<u>4,749,261,643</u>
Total Securities Lending	<u>.....</u>
<b>Total Investments (Settlement Date Basis)</b>	<u>4,749,261,643</u>
Due from Brokers - Securities Purchased But Not Settled, at Amortized Cost:	
U.S. Agency Discount Notes	398,222,667
Due to Brokers - Securities Sold But Not Settled, at Amortized Cost:	
U.S. Treasury Securities	<u>(398,324,597)</u>
<b>Total Investments (Trade Date Basis)</b>	<u>4,749,159,713</u>
Certificates of Deposit	444,050,000
Cash	(1,763,101)
Interest Receivable	2,877,953
Investment Trades Pending Receivable	<u>398,324,597</u>
<b>Total Assets</b>	<u>5,592,649,162</u>

### Liabilities

Accrued Expenses	41,077
Obligations under Securities Lending Agreement	<u>.....</u>
Investment Trades Pending Payable	<u>398,222,667</u>
<b>Total Liabilities</b>	<u>398,263,744</u>

### Net Assets

	<u>\$ 5,194,385,418</u>
Participant Net Asset Value, Price per Unit	<u>\$ 1.00</u>

Total Amortized Cost - Settlement Date Basis \$ 5,193,311,643

## QUARTER AT A GLANCE

January 1, 2002 - March 31, 2002

Total investment purchases:	\$ 23,173,127,169
Total investment sales:	\$ 1,266,409,510
Total investment maturities:	\$ 22,170,855,000
Total net income:	\$ 25,107,373
Net of realized gains and losses:	\$ 45,218
Net Portfolio yield (360-day basis):	
January	2.0675%
February	1.9092%
March	1.8420%
Average weighted days to maturity:	55 days

WASHINGTON STATE LOCAL GOVERNMENT INVESTMENT POOL  
OFFICE OF THE STATE TREASURER  
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